

Financial Statements
Manistee-Benzie Community
Mental Health Services

Manistee, Michigan

September 30, 2004



Auditing Procedures Report

Issued under P.A. 2 of 1968, as amended.

Local Government Type <input type="checkbox"/> City <input type="checkbox"/> Township <input type="checkbox"/> Village <input checked="" type="checkbox"/> Other		Local Government Name Manistee-Benzie Community Mental Health Ser	County Manistee
Audit Date 9/30/04	Opinion Date 12/16/04	Date Accountant Report Submitted to State: 3/28/05	

We have audited the financial statements of this local unit of government and rendered an opinion on financial statements prepared in accordance with the Statements of the Governmental Accounting Standards Board (GASB) and the *Uniform Reporting Format for Financial Statements for Counties and Local Units of Government in Michigan* by the Michigan Department of Treasury.

We affirm that:

1. We have complied with the *Bulletin for the Audits of Local Units of Government in Michigan* as revised.
2. We are certified public accountants registered to practice in Michigan.

We further affirm the following. "Yes" responses have been disclosed in the financial statements, including the notes, or in the report of comments and recommendations

You must check the applicable box for each item below.

- ☐ Yes ☒ No 1. Certain component units/funds/agencies of the local unit are excluded from the financial statements.
- ☐ Yes ☒ No 2. There are accumulated deficits in one or more of this unit's unreserved fund balances/retained earnings (P.A. 275 of 1980).
- ☒ Yes ☐ No 3. There are instances of non-compliance with the Uniform Accounting and Budgeting Act (P.A. 2 of 1968, as amended).
- ☐ Yes ☒ No 4. The local unit has violated the conditions of either an order issued under the Municipal Finance Act or its requirements, or an order issued under the Emergency Municipal Loan Act.
- ☐ Yes ☒ No 5. The local unit holds deposits/investments which do not comply with statutory requirements. (P.A. 20 of 1943, as amended [MCL 129.91], or P.A. 55 of 1982, as amended [MCL 38.1132]).
- ☐ Yes ☒ No 6. The local unit has been delinquent in distributing tax revenues that were collected for another taxing unit.
- ☐ Yes ☒ No 7. The local unit has violated the Constitutional requirement (Article 9, Section 24) to fund current year earned pension benefits (normal costs) in the current year. If the plan is more than 100% funded and the overfunding credits are more than the normal cost requirement, no contributions are due (paid during the year).
- ☐ Yes ☒ No 8. The local unit uses credit cards and has not adopted an applicable policy as required by P.A. 266 of 1995 (MCL 129.241).
- ☐ Yes ☒ No 9. The local unit has not adopted an investment policy as required by P.A. 196 of 1997 (MCL 129.95).

We have enclosed the following:

	Enclosed	To Be Forwarded	Not Required
The letter of comments and recommendations.	✓		
Reports on individual federal financial assistance programs (program audits).			✓
Single Audit Reports (ASLGU).			✓

Certified Public Accountant (Firm Name) Roslund, Prestage & Company, P.C.			
Street Address 308 Gratiot Avenue	City Alma	State MI	ZIP 48801
Accountant Signature <i>[Signature]</i>		Date 3/28/05	

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INDEPENDENT AUDITOR'S REPORT

Manistee-Benzie Community Mental Health Services
Manistee, Michigan

We have audited the accompanying financial statements of the governmental activities, each major fund, and the aggregate remaining fund information of Manistee-Benzie Community Mental Health Services (the Board), as of and for the year ended September 30, 2004, which collectively comprise the Board's basic financial statements as listed in the table of contents. These financial statements are the responsibility of the Board's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amount and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, each major fund, and the aggregate remaining fund information of the Board as of September 30, 2004, and the respective changes in financial position and cash flows, where applicable, for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued a report dated December 16, 2004 on our consideration of the Board's internal control over financial reporting and our test of its compliance with certain provisions of laws, regulations, contracts and grants. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be read in conjunction with this report in considering the results of our audit.

The Management's Discussion and Analysis on pages I - III and budgetary comparison information on page 25 are not a required part of the basic financial statements but are supplementary information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the supplementary information. However, we did not audit the information and express no opinion on it.

Our audit was made for the purpose of forming opinions on the financial statements that collectively comprise the Board's basic financial statements. The other supplemental information listed in the table of contents, is presented for purposes of additional analysis and is not a required part of the basic financial statements of the Board. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly stated in all material respects in relation to the basic financial statements taken as a whole.

Roslund, Prestage & Co, PC

Roslund, Prestage & Company, P.C.
Certified Public Accountants

December 16, 2004

MANAGEMENT'S DISCUSSION and ANALYSIS

Manistee Benzie Community Mental Health
Financial Statements for the Fiscal Year Ended September 30, 2004
Management's Discussion and Analysis

The management of Manistee Benzie Community Mental Health (MBCMH) presents the following overview and analysis of the financial activities during the past year. MBCMH was organized under an Urban Cooperation Act between the Board of Commissioners of Manistee County and Benzie County in 1992.

This discussion and analysis is provided to introduce the basic financial statements of the past year and to provide the reader information to help assess whether the financial position has improved or deteriorated as a result of the year's operation.

Basic Financial Statements -

Two types of financial statements are provided: Government-wide Financial Statements and Fund Financial Statements.

Government-wide financial statements are designed to present the organization's finances in a layout similar to that of a private sector business. They consist of a Statement of Net Assets (providing historical balance sheet information) which shows the difference between assets and liabilities; and a Statement of Activities (providing historical income statement information) which shows revenues and expenses and the change in net assets from the previous year.

Fund financial statements offer a series of statements that focus on the major governmental funds. For MBCMH, the major funds consist of the following funds: General, Building, Health, and Motor Pool. The Risk Management Fund was closed out during this current fiscal year due to discontinuance of risk insurance. Reconciliations are also offered between the Fund Financial Statements and the Government-wide Financial Statements.

Notes to Financial Statements:

The Notes to the Financial Statements, which immediately follow the Financial Statements, provide additional and more detailed information that is essential to a full understanding of the data provided in the Financial Statements.

The 2002/2003 fiscal year was the beginning of a contract period in which the Department of Community Health contracted for Medicaid services through a designated Prepaid Inpatient Health Plan (PIHP) which had to consist of 20,000 or more Medicaid covered lives. MBCMH, which has approximately 5,500 total Medicaid lives, entered into an affiliated cooperative agreement with Clinton Eaton Ingham Community Mental Health, Ionia County Community Mental Health, Newaygo County Community Mental Health, and Gratiot County Community Mental Health. This affiliation is called the Community Mental Health Affiliation of Mid-Michigan. Clinton Eaton Ingham Community Mental Health was designated as the PIHP in this cooperative agreement and was awarded the Medicaid contract for the 8 county region. Clinton Eaton Ingham Community Mental Health has sub-contracted with MBCMH to provide Medicaid covered services for the counties of Manistee and Benzie for the current fiscal year. The affiliation formed a base for working together to achieve administrative efficiencies and developing effective methodologies in delivering managed mental health services.

Manistee Benzie Community Mental Health also holds a Managed Mental Health Supports and Services Contract with the Department of Community Health for general funds.

The fiscal year 2003/2004 budget adopted by the governing board was \$14,052,979 of Revenues and \$14,339,158 Expenditures with use of fund balance of \$286,179 for the purchase of fixed assets. The Actual compared to Budget for the general fund is presented below.

	<u>Actual</u>	<u>Budget</u>	<u>Variance</u>
Revenue	\$13,699,856	\$14,052,979	\$(353,123)
Expenditures	\$14,120,672	\$14,339,158	\$218,486
Transfers In From Other Funds	\$216,816	\$-	\$216,816

The comparison of fiscal year 2003/2004 as compared to fiscal year 2002/2003 is presented below. These amounts are for the general fund of MBCMH.

	<u>2002/2003</u>	<u>2003/2004</u>	<u>Difference</u>
Revenues	\$13,849,799	\$13,699,856	\$(149,943)
Expenditures	\$13,796,187	\$14,120,672	\$324,485

The change in revenues recognized in the general fund between the 2003 and 2004 fiscal years was a decrease of 1%. Expenditures increased by 2.4%, mainly due to the purchase of an Electronic Medical Record Software Program, and substantial increases and updates to technology equipment.

For the 2003/2004 fiscal year the Department of Community Health revised the Medicaid funding distribution based on a regional rate. The Community Mental Health Affiliation of Mid-Michigan made the decision to continue to fund each affiliate based on the same percentage as the 2002/2003 fiscal year. This two year hold harmless period will end September 30, 2005. The new funding formula for the affiliation is currently being calculated. It is expected that Manistee Benzie Community Mental Health could see a substantial reduction in funding. In anticipation of the funding reduction for the 2006 fiscal year, current programs and services are being reviewed. It is expected that Community Mental Health Affiliation of Mid-Michigan will complete the funding plan for 2006 by mid March 2005.

**BASIC FINANCIAL STATEMENTS -
GOVERNMENT WIDE FINANCIAL STATEMENTS**

Manistee-Benzie Community Mental Health Services
Statement Of Net Assets
September 30, 2004 and 2003

	Governmental Activities	
	2004	2003
Assets		
Current assets		
Cash and cash equivalents	\$3,688,512	\$1,665,244
Investments	-	1,933,909
Accounts receivable, net	461,936	547,410
Due from other governmental units	216,659	134,665
Prepaid expenses	121,295	68,110
Total current assets	4,488,402	4,349,338
Noncurrent assets		
Capital assets - depreciable, net	1,462,263	1,854,079
Capital assets - land	122,000	150,300
Total noncurrent assets	1,584,263	2,004,379
Total assets	6,072,665	6,353,717
Liabilities		
Current liabilities		
Accounts payable	459,474	321,362
Accrued liabilities	164,454	183,472
Accrued payroll and related liabilities	467,036	452,950
Due to other governmental units	353,254	402,825
Land contract payable - current portion	-	60,056
Notes payable - current portion	82,722	199,132
Total current liabilities	1,526,940	1,619,797
Noncurrent liabilities		
Notes payable - less current portion	142,899	400,007
Total noncurrent liabilities	142,899	400,007
Total liabilities	1,669,839	2,019,804
Net Assets		
Invested in capital assets, net of related debt	1,358,642	1,345,184
Reserved for risk management	-	212,670
Unrestricted	3,044,184	2,776,059
Total net assets	\$4,402,826	\$4,333,913

The Notes to the Financial Statements are an integral part of this statement.

Manistee-Benzie Community Mental Health Services
Statement of Activities
For The Year Ended September 30, 2004 and 2003

Functions	Program Revenues			Net (Expense) Revenue and Changes Net Assets	2003
	Expenses	Charges for Services	Operating Grants and Contributions		
Governmental activities					
Health & Welfare - Mental Health	<u>\$13,716,703</u>	<u>11,817,425</u>	<u>1,834,793</u>	<u>(\$64,485)</u>	<u>(\$197,247)</u>
General revenues					
Unrestricted investment earnings				47,638	67,951
Restricted investment earnings				4,940	6,882
Internal service fund revenues, net of charges to the general fund				<u>80,820</u>	<u>86,377</u>
Total general revenues and contributions				<u>133,398</u>	<u>161,210</u>
Change in net assets				68,913	(36,037)
Net assets - beginning of year				<u>4,333,913</u>	<u>4,369,950</u>
Net assets - end of year				<u>\$4,402,826</u>	<u>\$4,333,913</u>

The Notes to the Financial Statements are an integral part of this statement.

FUND FINANCIAL STATEMENTS

Manistee-Benzie Community Mental Health Services
Balance Sheet
Governmental Funds
September 30, 2004 and 2003

	General Fund	
	2004	2003
Assets		
Cash and cash equivalents	\$3,549,913	\$1,565,383
Investments	-	1,721,239
Accounts receivable, net	453,965	547,086
Due from other funds	44,613	207,763
Due from other governmental units	216,659	129,520
Prepaid expenses	105,129	68,110
Total Assets	<u>\$4,370,279</u>	<u>\$4,239,101</u>
Liabilities and Fund Equity		
Liabilities		
Accounts payable	\$459,474	\$321,362
Accrued liabilities	111,268	86,564
Accrued payroll and related liabilities	467,036	452,950
Due to other governmental units	353,254	402,825
Due to other funds	207,847	-
Total liabilities	<u>1,598,879</u>	<u>1,263,701</u>
Fund equity		
Reserved for prepaid expenditures	105,129	68,110
Unreserved	2,666,271	2,907,290
Total fund equity	<u>2,771,400</u>	<u>2,975,400</u>
Total liabilities and fund equity	<u>\$4,370,279</u>	<u>\$4,239,101</u>

The Notes to the Financial Statements are an integral part of this statement.

Manistee-Benzie Community Mental Health Services
Reconciliation Of Fund Balances On The Balance Sheet For Governmental Funds
To Net Assets Of Governmental Activities On The Statement Of Net Assets
For The Year Ended September 30, 2004

Total fund balance - governmental funds	\$2,771,400
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Amounts reported for governmental activities in the statement of
net assets are different because:

Capital assets used in governmental activities are not financial resources
and therefore are not reported in the general fund.

Add: capital assets	600,358
Deduct: accumulated depreciation	(302,784)

Internal service funds are used by management to charge the costs of certain
activities, such as vehicle operations, building usage, and health benefits,
to individual funds. The assets and liabilities of the internal service
fund are included in the governmental activities in the statement of net assets.

1,333,852

Net assets of governmental activities

\$4,402,826

The Notes to the Financial Statements are an integral part of this statement.

Manistee-Benzie Community Mental Health Services
Statement Of Revenues, Expenditures And Changes In Fund Balances
Governmental Funds
For The Year Ended September 30, 2004 and 2003

	General Fund	
	2004	2003
REVENUES		
State Grants		
Department of Community Health Contract		
General Fund Formula And Categorical	\$1,241,117	\$1,365,963
Other State Grants	55,342	27,468
Total State Grants	<u>1,296,459</u>	<u>1,393,431</u>
Federal Grants	<u>159,283</u>	<u>151,914</u>
Contributions - Local Units		
County Appropriations	<u>279,273</u>	<u>275,205</u>
Charges For Services		
Medicaid - CEI CMH Contract	11,038,789	10,694,904
Medicaid - Other	117,499	128,246
Client And Third Party Pay	214,572	383,728
Other Contract Revenue	446,565	603,849
Total Charges For Services	<u>11,817,425</u>	<u>11,810,727</u>
Interest And Rents		
Interest	<u>47,638</u>	<u>67,951</u>
Other Revenue	<u>99,778</u>	<u>150,571</u>
Total Revenues	13,699,856	13,849,799
EXPENDITURES		
Health & Welfare - Mental Health		
Personnel Costs	7,032,409	6,881,606
Operating Expenditures	6,824,321	6,880,436
Capital Outlay	<u>263,942</u>	<u>34,145</u>
Total Expenditures	<u>14,120,672</u>	<u>13,796,187</u>
Excess Of Revenues Over Expenditures	(420,816)	53,612
Other Financing Sources (Uses)		
Operating Transfers In (Out)	<u>216,816</u>	<u>-</u>
Excess of Revenues and Other Financing Sources Over Expenditures and Other Financing Uses	(204,000)	53,612
Fund Balance, October 1	<u>2,975,400</u>	<u>2,921,788</u>
Fund Balance, September 30	<u>\$2,771,400</u>	<u>\$2,975,400</u>

The Notes to the Financial Statements are an integral part of this statement.

Manistee-Benzie Community Mental Health Services
Reconciliation Of The Statement Of Revenues, Expenditures
And Changes In Fund Balances Of Governmental Funds
To The Statement Of Activities
For The Year Ended September 30, 2004

Net change in fund balances - total governmental funds	(\$204,000)
Amounts reported for governmental activities in the statement of activities are different because:	
Governmental funds report capital outlays as expenditures. However, in the statement of activities, the cost of those assets is allocated over their estimated useful lives as depreciation expense.	
Add: capital outlay	263,942
Deduct: depreciation expense	(58,434)
Internal service funds are used by management to charge the costs of certain activities, such as vehicle operations, building usage, and health benefits, to the general fund. The net revenue (expense) of certain internal service funds is reported with governmental activities.	
	<u>67,405</u>
Change in net assets of governmental activities	<u><u>\$68,913</u></u>

The Notes to the Financial Statements are an integral part of this statement.

Manistee-Benzie Community Mental Health Services
Combined Statement Of Net Assets
Proprietary Funds
September 30, 2004 and 2003

	Internal Service Funds	
	2004	2003
Assets		
Current assets		
Cash and cash equivalents	\$138,599	\$99,861
Investments	-	212,670
Due from other funds	207,847	-
Due from other governmental units	-	5,145
Accounts receivable - other	7,971	324
Prepaid expenses	16,166	-
Total current assets	370,583	318,000
Noncurrent assets		
Capital assets - depreciable, net	1,164,689	1,762,013
Capital assets - land	122,000	150,300
Total noncurrent assets	1,286,689	1,912,313
Total assets	<u>\$1,657,272</u>	<u>\$2,230,313</u>
Liabilities and Net Assets		
Liabilities		
Current liabilities		
Due to other funds	\$44,613	\$207,763
Accrued liabilities	53,186	96,908
Land contract payable - current portion	-	60,056
Notes payable - current portion	82,722	199,132
Total current liabilities	180,521	563,859
Noncurrent liabilities		
Notes payable - less current portion	142,899	400,007
Total noncurrent liabilities	142,899	400,007
Total liabilities	323,420	963,866
Net Assets		
Contributed capital	11,071	11,071
Retained earnings		
Designated for catastrophic losses	-	212,670
Unreserved	1,322,781	1,042,706
Total net assets	1,333,852	1,266,447
Total liabilities and net assets	<u>\$1,657,272</u>	<u>\$2,230,313</u>

The Notes to the Financial Statements are an integral part of this statement.

Manistee-Benzie Community Mental Health Services
Combined Statement Of Revenues, Expenses And Changes In Fund Net Assets
Proprietary Funds
For The Year Ended September 30, 2004 and 2003

	<u>Internal Service Funds</u>	
	<u>2004</u>	<u>2003</u>
Operating revenues		
Charges for services and rent	\$1,587,887	\$1,279,934
Operating expenses		
Health claims	961,621	1,040,393
Vehicle expense	30,517	22,264
Depreciation	225,391	227,067
Maintenance	24,496	15,160
Insurance	8,083	11,767
Other	1,147	1,730
Total operating expenses	<u>1,251,255</u>	<u>1,318,381</u>
Operating income (loss)	336,632	(38,447)
Non-operating revenues (expenses)		
Interest income	4,940	6,882
Interest expenses	(42,366)	(39,528)
Gain/(loss) on sale of fixed assets	<u>(14,985)</u>	<u>-</u>
Total non-operating expense	<u>(52,411)</u>	<u>(32,646)</u>
Excess of revenues over expenditures	284,221	(71,093)
Other financing sources (uses)		
Operating transfers in (out)	<u>(216,816)</u>	<u>-</u>
Excess of revenues and other financing sources over expenditures and other financing uses	67,405	(71,093)
Net assets, beginning of year	<u>1,266,447</u>	<u>1,337,540</u>
Net assets, end of year	<u><u>\$1,333,852</u></u>	<u><u>\$1,266,447</u></u>

The Notes to the Financial Statements are an integral part of this statement.

Manistee-Benzie Community Mental Health Services
Combined Statement Of Cash Flows
Proprietary Funds
For The Year Ended September 30, 2004 and 2003

	Internal Service Funds	
	2004	2003
Cash flows from operating activities		
Receipts from interfund services provided	\$1,298,077	\$1,283,672
Receipts from others	84,510	116,103
Payments for interfund services	(168,198)	(557,305)
Payment to suppliers	(1,085,753)	(1,056,339)
Net cash provided (used) by operating activities	128,636	(213,869)
Cash flows from noncapital financial activities		
Operating transfers out	(216,816)	-
Cash flows from capital and related financing activities		
Principal paid on capital debt	(433,574)	(236,544)
Interest paid on capital debt	(42,366)	(39,528)
Proceeds from sales of capital assets	497,494	-
Purchase of capital assets	(112,246)	(152,071)
Net cash provided (used) by capital and related financing activities	(90,692)	(428,143)
Cash flows from investing activities		
Proceeds from maturity of investments	212,670	642,106
Proceeds from interest earnings	4,940	6,882
Net cash provided (used) by investing activities	217,610	648,988
Net increase (decrease) in cash and cash equivalents	38,738	6,976
Cash and cash equivalents, beginning of year	99,861	92,885
Cash and cash equivalents, end of year	<u>\$138,599</u>	<u>\$99,861</u>
Reconciliation of operating income to net cash provided by (used for) operating activities:		
Operating income (loss)	\$336,632	(\$38,447)
Adjustments to reconcile operating income to net cash provided (used) by operating activities		
Depreciation expense	225,391	227,067
(Increase) decrease in prepaid expenses	(16,166)	-
(Increase) decrease in due from other funds	(207,847)	86,482
(Increase) decrease in other receivables	(2,502)	33,358
Increase (decrease) in due to other funds	(163,150)	(557,305)
Increase (decrease) in accrued liabilities	(43,722)	34,976
Net cash provided (used) by operating activities	<u>\$128,636</u>	<u>(\$213,869)</u>

The Notes to the Financial Statements are an integral part of this statement.

Manistee-Benzie Community Mental Health Services
Statement of Fiduciary Net Assets
September 30, 2004 and 2003

	<u>Money Purchase Plan</u>	<u>Retirement Plan</u>	<u>2004</u>	<u>2003</u>
Assets				
Investments	<u>\$4,731,405</u>	<u>\$2,980,527</u>	<u>\$7,711,932</u>	<u>\$6,767,506</u>
Total assets	<u><u>\$4,731,405</u></u>	<u><u>\$2,980,527</u></u>	<u><u>\$7,711,932</u></u>	<u><u>\$6,767,506</u></u>
Liabilities And Net Assets				
Liabilities	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>
Net Assets Held in Trust for Pension Benefits	<u><u>\$4,731,405</u></u>	<u><u>\$2,980,527</u></u>	<u><u>\$7,711,932</u></u>	<u><u>\$6,767,506</u></u>

The Notes to the Financial Statements are an integral part of this statement.

Manistee-Benzie Community Mental Health Services
Statement of Changes in Fiduciary Net Assets
For The Year Ended September 30, 2004 and 2003

	Money Purchase Plan	Retirement Plan	2004	2003
Additions				
Contributions				
Employer contributions	\$329,323	\$267,293	\$596,616	\$611,918
Employee contributions	-	267,293	267,293	290,498
Total contributions	329,323	534,586	863,909	902,416
Investment Earnings				
Net increase (decrease) in fair value of investments	617,823	(34,797)	583,026	1,125,740
Total additions	947,146	499,789	1,446,935	2,028,156
Deductions				
Administrative and general expenses	(4,939)	-	(4,939)	(5,361)
Benefit payments and refunds	(497,570)	-	(497,570)	(159,855)
Total deductions	(502,509)	-	(502,509)	(165,216)
Change in net assets	444,637	499,789	944,426	1,862,940
Net assets - beginning of year	4,286,768	2,480,738	6,767,506	4,904,566
Net assets - end of year	\$4,731,405	\$2,980,527	\$7,711,932	\$6,767,506

The Notes to the Financial Statements are an integral part of this statement.

NOTES TO THE FINANCIAL STATEMENTS

Manistee-Benzie Community Mental Health Services
Notes To The Financial Statements

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The accounting policies of the Manistee-Benzie Community Mental Health Services (the Board) conform to accounting principles generally accepted in the United States of America as applicable to governmental units. The Governmental Accounting Standards Board (GASB) is the accepted standard-setting body for establishing governmental accounting and financial reporting principles. The following is a summary of the significant accounting policies used by the Board.

In June of 1999, the GASB issued Statement No. 34, *Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments*. The significant changes included in Statement No. 34 include the following:

- A Management's Discussion and Analysis (MD&A) section providing an analysis of the Board's overall financial position and results of operations.
- Financial statements prepared using full accrual accounting for all of the Board's activities
- A change in the fund financial statements to focus on major funds.

These and other changes are reflected in the accompanying financial statements (including the notes to the financial statements). The Board has implemented the provisions of Statement No. 34 effective October 1, 2002.

A. Reporting Entity

The Board is organized under the Urban Cooperation Act of 1967 as a Community Mental Health Organization (330.1204) (Act 258 of the Public Acts of 1974, as amended).

The Board provides funding for services in the areas of mental illness, developmental disabilities, and other related mental health needs for residents of Manistee and Benzie Counties.

The accompanying financial statements have been prepared in accordance with criteria established by the Governmental Accounting Standards Board for determining the various governmental organizations to be included in the reporting entity. These criteria include significant operational financial relationships that determine which of the governmental organizations are a part of the Board's reporting entity, and which organizations are legally separate, component units of the Board. Based on the application of the criteria, the Board does not contain any component units.

Manistee-Benzie Community Mental Health Services
Notes To The Financial Statements

B. Government-Wide and Fund Financial Statements

The government-wide financial statements (i.e. the statement of net assets and the statement of activities) report information on all of the non-fiduciary activities of the Board. For the most part, the effect of interfund activity has been removed from these statements. *Governmental activities*, which normally are supported by taxes and intergovernmental revenues, are reported separately from business-type activities, which rely to a significant extent on fees and charges for support.

The statement of activities demonstrates the degree to which the direct expenses of a function are offset by program revenues. Direct expenses are those that are clearly identifiable with a specific function. Program revenues include charges to consumers who purchase, use or directly benefit from services provided by a given function. Program revenues also include grants and contributions that are restricted to meeting the operational or capital requirements of a particular function. Other items not properly included among program revenues are reported instead as general revenues. Resources that are dedicated internally are reported as general revenues rather than as program revenues.

Net assets are restricted when constraints placed on them are either externally imposed or are imposed by constitutional provisions or enabling legislation. Internally imposed designations of resources are not presented as restricted net assets. When both restricted and unrestricted resources are available for use, generally it is the Board's policy to use restricted resources first, then unrestricted resources as they are needed.

Separate financial statements are provided for governmental funds and proprietary funds. Major individual governmental funds are reported as separate columns in the fund financial statements.

C. Measurement Focus, Basis of Accounting and Financial Statement Presentation

Government-Wide Financial Statements – The government-wide financial statements are reported using the economic resources measurement focus and the accrual basis of accounting. Revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows. Grants and similar items are recognized as revenue as soon as all eligibility requirements imposed by the provider have been met.

Manistee-Benzie Community Mental Health Services
Notes To The Financial Statements

Governmental Fund Financial Statements - The governmental fund financial statements are reported using the current financial resources measurement focus and the modified accrual basis of accounting. Revenues are recognized as soon as they are both measurable and available. Revenues are considered to be available when they are collectible within the current period or soon enough thereafter to pay liabilities of the current period. For this purpose, the Board considers revenues to be available if they are collected within 60 days of the end of the current fiscal year end. Expenditures generally are recorded when a liability is incurred, as under accrual accounting.

Modifications to the accrual basis of accounting include:

- Interest on general long-term obligations is recognized when paid.
- Debt service expenditures and claims and judgments are recorded only when payment is due.

Proprietary Fund Financial Statements - The financial statements of the proprietary funds are reported using the economic resources measurement focus and the accrual basis of accounting, similar to the government-wide statements described above.

Private-sector standards of accounting and financial reporting issued prior to December 1, 1989, are followed to the extent that those standards do not conflict with or contradict guidance of the Governmental Accounting Standards Board.

As a general rule the effect of interfund activity has been eliminated from the government-wide financial statements.

Proprietary funds distinguish operating revenues and expenses from non-operating items. Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with a proprietary fund's principal ongoing operations. Revenues and expenses not meeting this definition are reported as non-operating revenues and expenses. The principal operating revenues of the internal service fund are charges to the general fund for vehicle operations, building operations, and insurance services. Operating expenses for internal service funds include vehicle operations, building operations, and insurance claims. Any revenues and expenses not meeting this definition are reported as non-operating revenues and expenses.

Manistee-Benzie Community Mental Health Services
Notes To The Financial Statements

The Board reports the following major governmental and proprietary funds:

Governmental Funds

General Fund – This fund is the Board's primary operating fund. It accounts for all financial resources of the Board, except those required to be accounted for in other funds.

Proprietary Funds

Internal Service Funds – These funds are used to account for the financing of goods or services provided by one department or agency to other departments or agencies or to other governments on a cost-reimbursement basis. The Risk Management Fund was established on October 1, 1998 to finance exposure to risk under managed care contracts. The Motor Pool Fund, Building Fund and Health Fund are also reported as Internal Service Funds.

Fiduciary Funds

Pension Trust Funds – These funds account for assets for which the Board is responsible as a trustee under the employee's two retirement plans.

D. Comparative Data

Comparative total data for the prior year has been presented in order to provide an understanding of the changes in financial position and operations. Also, certain amounts presented in the prior year may have been reclassified in order to be consistent with the current year's presentation.

E. Budgetary Data

Budgets are adopted by the Board for all governmental funds. The budget is adopted and prepared on the modified accrual basis of accounting. The budget is also adopted at the function level. The budgeted revenues and expenditures for governmental fund types, as presented in this report, include any authorized amendments to the original budget as adopted.

Manistee-Benzie Community Mental Health Services
Notes To The Financial Statements

F. Cash and Cash Equivalents

The Board's cash and cash equivalents are considered to be cash on hand, money market funds, demand deposits and certificates of deposit.

Michigan Compiled Laws, Section 129.91, authorized the Board to deposit and invest in the accounts of Federally insured banks, credit unions, and savings and loan associations; bonds, securities and other direct obligations of the United States, or any agency or instrumentality of the United States; United States government or Federal agency obligation repurchase agreements; bankers' acceptance of United States banks; commercial paper rated by two standard rating agencies within the two highest classifications, which mature not more than 270 days after the date of purchase; obligations of the State of Michigan or its political subdivisions which are rated investment grade; and mutual funds composed of investment vehicles which are legal for direct investment by local units of government in Michigan.

G. Receivables and Payables between Funds

Activity between funds that are representative of lending / borrowing arrangements outstanding at the end of the fiscal year are referred to as either "due to / from other funds" (i.e. the current portion of interfund loans) or "advances to / from other funds" (i.e. the non-current portion of interfund loans). All other outstanding balances between funds are reported as "due to / from other funds". Any residual balances outstanding between the governmental activities are reported in the government-wide financial statements as "internal balances".

H. Receivables

Accounts receivable in all funds report amounts that have arisen in the ordinary course of business and are stated net of allowances for uncollectible amounts.

Due from other governmental entities consist primarily of amounts due from the Michigan Department of Community Health and the State of Michigan.

I. Inventories

The Board does not recognize as an asset inventories of supplies. The cost of these supplies is considered immaterial to the financial statements and the quantities are not prone to wide fluctuation from year to year. The costs of such supplies are expensed when purchased.

J. Prepaid Items

Certain payments to vendors reflect costs applicable to future accounting periods and are recorded as prepaid items in both government-wide and fund financial statements.

Manistee-Benzie Community Mental Health Services
Notes To The Financial Statements

K. Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenditures during the reporting period. Actual results could differ from those estimates.

L. Capital Assets

Capital assets, which include property, plant and equipment, are reported in the governmental activities column in the government-wide financial statements. Capital assets are defined by the government as individual assets with an initial cost equal to or more than \$5,000 and an estimated useful life in excess of one year. Such assets are recorded at historical cost or estimated historical cost if purchased or constructed. Donated capital assets are recorded at estimated fair value at the date of donation.

The costs of normal maintenance and repairs that do not add to the value of the asset or materially extend asset lives are not capitalized.

Major outlays for capital assets and improvements are capitalized as projects are constructed. Interest incurred during construction of capital assets is not capitalized. No interest expense was incurred during the current year.

Capital assets utilized in the governmental funds are recorded as expenditures in the governmental fund financial statements. Depreciation expense is recorded in the government-wide financial statements and proprietary fund financial statements. Computers, software and building and improvements are depreciated using the straight-line method over their estimated useful lives. Vehicles are depreciated using an accelerated method over their estimated useful lives. Following is a breakdown of estimated useful lives used:

Assets	Years
Computers	5
Software	3
Automobiles	5
Buildings and Improvements	7-40
Land	Not Applicable - Not Depreciated

Manistee-Benzie Community Mental Health Services
Notes To The Financial Statements

M. Compensated Absences

Paid time off is valued using a vesting schedule based on each employee's years of service ranging from 160 hours during the first year to 320 hours after ten years. Paid time off may not be carried over from one fiscal year to the next and it may not be advanced from a future fiscal year into a current fiscal year. Therefore, the government-wide financial statements do not present a cost for compensated absences as a liability.

Each employee has the option to "sell back" up to half of the annual paid time off, to be paid at the current pay rate for that fiscal year. The payment may be taken as compensation or may be deferred into a tax-free investment.

At the time of termination, no more than half of the paid time off granted during a fiscal year will be paid as compensation.

N. Governmental Fund – Fund Balance Reserves and Designations

The governmental fund financial statements present fund balance reserves for those portions of fund balance (1) not available for appropriation for expenditure or (2) legally segregated for a specific future use. The reserves for related assets such as prepaid items are examples of the former. Reserves for risk management are an example of the latter.

O. Inpatient / Residential Cost Liability

The amount recorded for inpatient/residential liability is based on management's estimate. This estimate is based on 1) the number of clients at each facility, 2) the number of days each client is at each facility, and 3) the daily rate charged for each facility.

The Board does not receive actual billings for these services until several months after the service date. Therefore, the liability is not liquidated within the normal 60 day period after year end. Also, the actual cost may vary from the estimated due to reimbursements from third party payors that are applied to the total cost before the billings are sent to the Board.

NOTE 2 - STEWARDSHIP, COMPLIANCE AND ACCOUNTABILITY

A. Budgetary Information

Annual budgets are adopted at the function level and on a basis consistent with accounting principles generally accepted in the United States of America for the General fund. All annual appropriations lapse at fiscal year end. The Board does not maintain a formalized encumbrance accounting system.

Manistee-Benzie Community Mental Health Services
Notes To The Financial Statements

B. Excess of Expenditures over Appropriations

P.A. 621 of 1978, Section 18 (1), as amended, provides that a local unit shall not incur expenditures in excess of the amount appropriated.

Budgets for the budgetary funds were adopted on a function level and have been presented as such on page 25.

During the year ended September 30, 2004, the Board incurred expenditures in excess of the amounts appropriated as shown on page 25.

NOTE 3 - DETAIL NOTES

A. Deposits and Investments

At year end, the carrying amount of deposits for the Board was \$3,688,512, and the bank balance was \$3,904,180. Of the bank balance, \$300,000 was covered by federal depository insurance and the remaining, was uninsured and uncollateralized.

The Board believes that due to the dollar amounts of cash deposits and the limits of FDIC insurance, it is impractical to insure all bank deposits. As a result, the Board evaluates each financial institution with which it deposits government funds and accesses the level of risk of each institution. Only those institutions with an acceptable estimated risk level are used as depositories.

The Board's investments can be classified into three categories to give an indication of the level of risk assumed. Category 1 includes investments that are insured or registered or securities held by the Board or its agent in the Board's name. Category 2 includes uninsured and unregistered investments, which are held by the counterparty's, trust department or agent in the Board's name. Category 3 includes uninsured and unregistered investments for which the securities are held by a counterparty's trust department or agent but not in the Board's name.

Manistee-Benzie Community Mental Health Services
Notes To The Financial Statements

The Board's investments held at September 30, 2003 are classified as follows. There were no investments as of September 30, 2004.

Investment	Category 1	Category 2	Carrying Value	Market Value
Fannie Mae Notes		\$512,800	\$512,800	\$512,800
Certificate of Deposit	\$882,555		882,555	882,555
Uncategorized: - Money Market Mutual Funds			538,554	538,554
Totals	\$882,555	\$512,800	\$1,933,909	\$1,933,909

B. Due From Other Governmental Units

Due from other governmental units as of September 30, consists of the following:

Governmental Unit	2004	2003
Michigan Department of Community Health - OBRA Grant	\$18,825	\$32,211
Michigan Department of Community Health - Wraparound Grant	25,237	-
Benzie County	28,568	53,068
Manistee County	13,750	-
Clinton, Eaton, Ingham CMH Authority	68,922	-
Manistee Intermediate School District	11,825	10,000
Various Other Governmental Units	49,532	39,386
Total	\$216,659	\$134,665

Manistee-Benzie Community Mental Health Services
Notes To The Financial Statements

C. Capital Assets

A summary of changes in the Board's capital assets follows:

Governmental Activities	Beginning Balance	Additions	Disposals	Ending Balance
Computers / Office Equipment	\$193,886	\$85,347		\$279,233
Software	142,531	178,595		321,126
Automobiles	577,450	90,496	(\$52,410)	615,536
Buildings and Improvements	2,305,732	19,750	(701,123)	1,624,359
Land	150,300	2,000	(30,300)	122,000
Sub-totals	3,369,899	376,188	(783,833)	2,962,254
Accumulated Depreciation	(1,365,520)	(283,822)	271,351	(1,377,991)
Totals	\$2,004,379	\$92,366	(\$512,482)	\$1,584,263

Depreciation expense was charged to the Health & Welfare – Mental Health Program.

D. Accrued Wages and Other Payroll Liabilities

This liability represents amounts paid to employees during October that was earned during September or before. Also included are employer payroll taxes.

E. Due To Other Governmental Units

As of September 30, this liability consists of the following:

Governmental Unit	2004	2003
State of Michigan – Inpatient/Residential Care	\$53,264	\$91,908
State of Michigan – Cost Settlement	3,672	3,672
Clinton, Eaton, Ingham CMH Authority	248,126	266,687
Other Governmental Units	48,192	40,558
Total	\$353,254	\$402,825

Manistee-Benzie Community Mental Health Services
Notes To The Financial Statements

F. Long Term Liabilities

The Building Fund purchased land and a building from Maple Street Development on a land contract. The contract is payable in monthly installments of \$8,139 with an interest rate of 5.5% and is secured by real estate. The loan was paid in full during the 2004 fiscal year.

The Building Fund financed the purchase of land and a building with a bank. The note is payable in monthly installments of \$1,608 with an interest rate of 7.9% and is secured by real estate. The building was sold during the 2004 fiscal year and this note was paid in full during the 2004 fiscal year.

The Building Fund financed \$500,000 for the purchase and renovation of land and a building with a bank. The note is payable in monthly installments of \$5,698 with an interest rate of 6.58% and is secured by real estate. The building was sold during the 2004 fiscal year and this note was paid in full during the 2004 fiscal year.

The Building Fund financed \$395,000 for the purchase and renovation of land and a building with a bank. The note is payable in monthly installments of \$4,501 with an interest rate of 6.58% and is secured by real estate. The balance owed at September 30, 2004 was \$72,466.

The Building Fund financed \$300,000 for an addition to the Administrative Building with a bank. The note is payable in monthly installments of \$3,399 with an interest rate of 6.36% and is secured by real estate. The balance owed at September 30, 2004 was \$153,155.

The changes in long term liabilities during the 2004 fiscal year are as follows:

Liability	Balance October 1 st	Additions	Reductions	Balance September 30 th
Land contract	\$60,056	\$-	\$60,056	\$-
Notes	599,139	-	373,518	225,621

The annual installments to pay principal and interest on obligations outstanding at September 30, 2004 are as follows, including total interest payments of \$25,900.

Year Ended September 30,	Notes Payable
2005	
2006	\$94,797
2007	62,820
2008	40,782
2009	40,782
2010 & Thereafter	12,340
	-

Manistee-Benzie Community Mental Health Services
Notes To The Financial Statements

NOTE 4 - OTHER INFORMATION

A. Risk Management

Michigan Municipal Risk Management Authority

The Board is exposed to risks of loss related to theft of, damage to, and destruction of assets; errors and omissions; injuries to employees; and natural disasters. The Board manages its risk exposures and provides certain employee benefits through a combination of self-insurance, risk management pools and commercial insurance. Except as described below, coverage provided by pools and commercial carriers has not changed significantly and there have been no claims paid in excess of insured limits in the past three years.

The Board participated in the public entity risk pool – Michigan Municipal Risk Management Authority (MMRMA) for general liability and property damage coverage.

MMRMA, a separate legal entity, is a self-insured association organized under the laws of the State of Michigan to provide self-insurance protection against loss and risk management services to various Michigan governmental entities.

As a member of this pool, the Board is responsible for paying all losses, including damages, loss adjustment expenses and defense costs, for each occurrence that falls within the member's self-insured retention. If a covered loss exceeds MMRMA's limits, all further payments for such loss are the sole obligation of the Board. If for any reason, the MMRMA's resources available to pay losses are depleted, the payment of all unpaid losses of the Board is the sole obligation of the Board.

Internal Service Funds

In a previous year, the Board authorized the establishment of an Internal Service Fund used to cover the risk of overspending the Managed Care Specialty Services Program (MCSSP) contract. This contract provides for the use of Department of Community Health funding for the establishment of an Internal Service Fund, which is restricted to meet the expected future risk corridor requirements of the contract. Expenditures from the Internal Service Fund will occur when, in any one fiscal year, the Board finds it necessary to expend more to provide services necessary to carry out the MCSSP contract requirements than revenue provided to the Board by the contract.

Self-Insured Medical Benefits

The Board has established a self-insurance plan covering certain medical, dental and vision benefits for substantially all of its employees. An internal service fund has been established to pay benefit claims and is funded by the Special revenue fund based on projected claims. The Board maintains specific stop-loss coverage of \$40,000 per person each year.

Manistee-Benzie Community Mental Health Services
Notes To The Financial Statements

Estimates for the liability for unpaid claims are based on actual claims in process as of the year end. Incurred, but unreported, claims are estimated by management to be insignificant.

B. Retirement System

Money Purchase Pension Plan

Manistee-Benzie Community Mental Health Services sponsors a Money Purchase Pension Plan (the "Plan"). The Plan is a tax-qualified defined contribution pension plan. Employees of the Board are generally eligible to participate in the Plan ("eligible employee") as of the July 1 or January 1 following their attainment of age 18 and completion of six months of service. The Board contributes an amount to each participant's account equal to 7% of the participant's compensation. This amount is allocated following the end of each Plan year to all participants. The Board's contribution for the year ended September 30, 2004 and 2003 was \$329,323 and \$322,179, respectively.

Contributions made to the Plan are held in a Trust Fund. The trust assets do not belong to the Board but are held for the exclusive benefit of Plan participants and beneficiaries. It is the duty of the Trustees to administer the Trust Fund.

Retirement Investment Plan

Manistee-Benzie Community Mental Health Services established a thrift plan effective January 1, 1998, under the Employee Retirement Income Security Act of 1974. An employee becomes eligible to participate on their first date of employment. As a condition of employment, each participant must agree to contribute 6.2% of his or her compensation to the plan. The Board contributes an amount equal to 100% of the aggregate employee contributions. The Employer Contribution Account is fully vested at all times; however, withdrawals from the plan are not allowed prior to termination of employment.

C. Compliance Audits

All governmental grants are subject to a transactional and compliance audit by the grantors or their representatives. Therefore, an indeterminable contingency exists for expenditures, which may be disallowed by the granting agencies.

REQUIRED SUPPLEMENTAL INFORMATION

Manistee-Benzie Community Mental Health Services
Statement Of Revenues, Expenditures And Changes
In Fund Balance - Budget And Actual
General Fund
For The Year Ended September 30, 2004

	Budgeted Amounts			Variance Between Actual and Final Budget
	Original	Final	Actual	
REVENUES				
State Grants				
Department of Community Health Contract				
General Fund Formula And Categorical	\$1,308,920	\$1,244,789	\$1,241,117	\$ (3,672)
Other State Grants	63,648	66,248	55,342	(10,906)
Total State Grants	<u>1,372,568</u>	<u>1,311,037</u>	<u>1,296,459</u>	<u>(14,578)</u>
Federal Grants	<u>145,147</u>	<u>155,500</u>	<u>159,283</u>	<u>3,783</u>
Contributions - Local Units				
County Appropriations	<u>263,000</u>	<u>279,273</u>	<u>279,273</u>	<u>-</u>
Charges For Services				
Medicaid - CEI CMH Contract	10,801,491	11,257,080	11,038,789	(218,291)
Medicaid - Other	132,100	123,446	117,499	(5,947)
Client And Third Party Pay	459,933	353,873	214,572	(139,301)
Other Contract Revenue	401,189	416,770	446,565	29,795
Total Charges For Services	<u>11,794,713</u>	<u>12,151,169</u>	<u>11,817,425</u>	<u>(333,744)</u>
Interest And Rents				
Interest	<u>40,000</u>	<u>50,000</u>	<u>47,638</u>	<u>(2,362)</u>
Other Revenue	<u>120,000</u>	<u>106,000</u>	<u>99,778</u>	<u>(6,222)</u>
Total Revenues	13,735,428	14,052,979	13,699,856	(353,123)
EXPENDITURES				
Health & Welfare - Mental Health				
Personnel Costs	6,992,833	7,228,494	7,032,409	196,085
Operating Expenditures	6,732,595	6,876,713	6,824,321	52,392
Capital Outlay	-	233,951	263,942	(29,991)
Total Expenditures	<u>13,725,428</u>	<u>14,339,158</u>	<u>14,120,672</u>	<u>218,486</u>
Excess Of Revenues Over Expenditures	10,000	(286,179)	(420,816)	(134,637)
Other Financing Sources (Uses)				
Operating Transfers In (Out)	<u>-</u>	<u>-</u>	<u>216,816</u>	<u>216,816</u>
Excess of Revenues and Other Financing Sources Over Expenditures and Other Financing Uses	10,000	(286,179)	(204,000)	82,179
Fund Balance, October 1	<u>2,975,400</u>	<u>2,975,400</u>	<u>2,975,400</u>	<u>-</u>
Fund Balance, September 30	<u>\$2,985,400</u>	<u>\$2,689,221</u>	<u>\$2,771,400</u>	<u>\$82,179</u>

The Notes to the Financial Statements are an integral part of this statement.

OTHER SUPPLEMENTAL INFORMATION

Manistee-Benzie Community Mental Health Services
Supporting Schedule of Personnel Costs
For The Year Ending September 30, 2004 and 2003

Governmental Fund Types

General Fund

	<u>2004</u>	<u>2003</u>
Personnel Costs		
Salaries and wages	\$5,208,192	\$5,255,023
Fringe benefits	<u>1,824,217</u>	<u>1,626,583</u>
Total personnel costs	<u><u>\$7,032,409</u></u>	<u><u>\$6,881,606</u></u>

The Notes to the Financial Statements are an integral part of this statement.

Manistee-Benzie Community Mental Health Services
Supporting Schedule of Operating Expenditures
For The Year Ending September 30, 2004 and 2003

Governmental Fund Types

General Fund

Operating Expenditures	<u>2004</u>	<u>2003</u>
Contractual services	\$4,896,441	\$5,076,847
Client supplies	45,399	53,766
Insurance	88,629	222,280
MSHDA grant expense	41,572	7,000
Office and computer supplies	18,313	31,008
Operating supplies	90,210	108,500
Other	44,538	31,356
Rent	454,638	403,843
Repairs and maintenance	280,572	207,026
Small equipment purchases	196,739	77,807
Staff development and training	52,051	61,565
Telephone and utilities	191,685	177,979
Transportation	82,066	87,158
Travel	341,468	334,301
	<u>341,468</u>	<u>334,301</u>
Total operating expenditures	<u><u>\$6,824,321</u></u>	<u><u>\$6,880,436</u></u>

The Notes to the Financial Statements are an integral part of this statement.

Manistee-Benzie Community Mental Health Services
Combining Statement Of Net Assets
Proprietary Funds
September 30, 2004 and 2003

	Risk Management Fund	Motor Pool Fund	Building Fund	Health Fund	Internal Service Funds	
					2004	2003
Assets						
Current assets						
Cash and cash equivalents	-	-	-	\$138,599	\$138,599	\$99,861
Investments	-	-	-	-	-	212,670
Due from other funds	-	-	\$207,847	-	207,847	-
Due from other governmental units	-	-	-	-	-	5,145
Accounts receivable - other	-	-	7,971	-	7,971	324
Prepaid expenses	-	\$16,166	-	-	16,166	-
Total current assets	-	16,166	215,818	138,599	370,583	318,000
Noncurrent assets						
Capital assets - depreciable, net	-	188,640	976,049	-	1,164,689	1,762,013
Capital assets - land	-	-	122,000	-	122,000	150,300
Total noncurrent assets	-	188,640	1,098,049	-	1,286,689	1,912,313
Total assets	-	\$204,806	\$1,313,867	\$138,599	\$1,657,272	\$2,230,313
Liabilities and Net Assets						
Liabilities						
Current liabilities						
Due to other funds	-	\$18,914	-	\$25,699	\$44,613	\$207,763
Accrued liabilities	-	-	-	53,186	53,186	96,908
Land contract payable - current portion	-	-	-	-	-	60,056
Notes payable - current portion	-	-	\$82,722	-	82,722	199,132
Total current liabilities	-	18,914	82,722	78,885	180,521	563,859
Noncurrent liabilities						
Notes payable - less current portion	-	-	142,899	-	142,899	400,007
Total noncurrent liabilities	-	-	142,899	-	142,899	400,007
Total liabilities	-	18,914	225,621	78,885	323,420	963,866
Net Assets						
Contributed capital	-	11,071	-	-	11,071	11,071
Retained earnings	-	-	-	-	-	212,670
Designated for catastrophic losses	-	-	-	-	-	1,042,706
Unreserved	-	174,821	1,088,246	59,714	1,322,781	1,042,706
Total net assets	-	185,892	1,088,246	59,714	1,333,852	1,266,447
Total liabilities and net assets	-	\$204,806	\$1,313,867	\$138,599	\$1,657,272	\$2,230,313

The Notes to the Financial Statements are an integral part of this statement.

Manistee-Benzie Community Mental Health Services
Combining Statement Of Revenues, Expenses And Changes In Fund Net Assets
Proprietary Funds
For The Year Ended September 30, 2004 and 2003

	Risk Management Fund	Motor Pool Fund	Building Fund	Health Fund	Internal Service Funds	
					2004	2003
Operating revenues						
Charges for services	-	\$154,057	-	\$1,120,744	\$1,274,801	\$959,957
Rent	-	-	\$313,086	-	313,086	319,977
Total operating revenues	-	154,057	313,086	1,120,744	1,587,887	1,279,934
Operating expenses						
Health claims	-	-	-	961,621	961,621	1,040,393
Vehicle expense	-	30,517	-	-	30,517	22,264
Depreciation	-	102,676	122,715	-	225,391	227,067
Maintenance	-	24,496	-	-	24,496	15,160
Insurance	-	8,083	-	-	8,083	11,767
Other	-	1,147	-	-	1,147	1,730
Total operating expenses	-	166,919	122,715	961,621	1,251,255	1,318,381
Operating income (loss)	-	(12,862)	190,371	159,123	336,632	(38,447)
Non-operating revenues (expense)						
Interest income	4,146	-	-	794	4,940	6,882
Interest expenses	-	-	(42,366)	-	(42,366)	(39,528)
Gain/(loss) on sale of fixed assets	-	6,183	(21,168)	-	(14,985)	-
Total non-operating revenues (expense)	4,146	6,183	(63,534)	794	(52,411)	(32,646)
Excess of revenues over expenditures	4,146	(6,679)	126,837	159,917	284,221	(71,093)
Other financing sources (uses)						
Operating transfers in (out)	(216,816)	-	-	-	(216,816)	-
Excess of revenues and other financing sources over expenditures and other financing uses	(212,670)	(6,679)	126,837	159,917	67,405	(71,093)
Net assets, beginning of year	212,670	192,571	961,409	(100,203)	1,266,447	1,337,540
Net assets, end of year	\$ -	\$185,892	\$1,088,246	\$59,714	\$1,333,852	\$1,266,447

The Notes to the Financial Statements are an integral part of this statement.

Manistee-Benzie Community Mental Health Services
Combining Statement Of Cash Flows
Proprietary Funds
For The Year Ended September 30, 2004 and 2003

	Risk Management Fund	Motor Pool Fund	Building Fund	Health Fund	Internal Service Funds	
					2004	2003
Cash flows from operating activities						
Receipts from interfund services provided	-	\$148,647	\$29,385	\$1,120,045	\$1,298,077	\$1,283,672
Receipts from others	-	10,458	73,352	700	84,510	116,103
Payments for interfund services	-	-	(90,741)	(77,457)	(168,198)	(557,305)
Payment to suppliers	-	(80,409)	-	(1,005,344)	(1,085,753)	(1,056,339)
Net cash provided (used) by operating activities	-	78,696	11,996	37,944	128,636	(213,869)
Cash flows from noncapital financial activities						
Operating transfers out	(\$216,816)	-	-	-	(216,816)	-
Cash flows from capital and related financing activities						
Principal paid on capital debt	-	-	(433,574)	-	(433,574)	(236,544)
Interest paid on capital debt	-	-	(42,366)	-	(42,366)	(39,528)
Proceeds from sales of capital assets	-	11,800	485,694	-	497,494	-
Purchase of capital assets	-	(90,496)	(21,750)	-	(112,246)	(152,071)
Net cash provided (used) by capital and related financing activities	-	(78,696)	(11,996)	-	(90,692)	(428,143)
Cash flows from investing activities						
Proceeds from maturity of investments	212,670	-	-	-	212,670	642,106
Proceeds from interest earnings	4,146	-	-	794	4,940	6,882
Net cash provided (used) by investing activities	216,816	-	-	794	217,610	648,988
Net increase (decrease) in cash and cash equivalents	-	-	-	38,738	38,738	6,976
Cash and cash equivalents, beginning of year	-	-	-	99,861	99,861	92,885
Cash and cash equivalents, end of year	-	-	-	\$138,599	\$138,599	\$99,861
Reconciliation of operating income to net cash provided by (used for) operating activities:						
Operating income (loss)	-	(\$12,862)	\$190,371	\$159,123	\$336,632	(\$38,447)
Adjustments to reconcile operating income to net cash provided (used) by operating activities						
Depreciation expense	-	102,676	122,715	-	225,391	227,067
(Increase) decrease in prepaid expenses	-	(16,166)	-	-	(16,166)	-
(Increase) decrease in due from other funds	-	-	(207,847)	-	(207,847)	86,482
(Increase) decrease in other receivables	-	-	(2,502)	-	(2,502)	33,358
Increase (decrease) in due to other funds	-	5,048	(90,741)	(77,457)	(163,150)	(557,305)
Increase (decrease) in accrued liabilities	-	-	-	(43,722)	(43,722)	34,976
Net cash provided (used) by operating activities	-	\$78,696	\$11,996	\$37,944	\$128,636	(\$213,869)

The Notes to the Financial Statements are an integral part of this statement.



**REPORT ON COMPLIANCE AND ON INTERNAL CONTROL
OVER FINANCIAL REPORTING BASED ON AN AUDIT OF
FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH
GOVERNMENT AUDITING STANDARDS**

Manistee-Benzie Community Mental Health Services
Manistee, Michigan

We have audited the financial statements of the governmental activities, each major fund, and the aggregate remaining fund information of Manistee-Benzie Community Mental Health Services (the Board) as of and for the year ended September 30, 2004, which collectively comprise the Board's basic financial statements and have issued our report thereon dated December 16, 2004. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States.

Compliance

As part of obtaining reasonable assurance about whether the Board's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grants, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance that are required to be reported under *Government Auditing Standards*.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the Board's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide assurance on the internal control over financial reporting. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control over financial reporting that might be material weaknesses.

A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions.

We noted no matters involving the internal control over financial reporting and its operation that we consider to be material weaknesses. However, we noted other matters involving the internal control over financial reporting that we have reported to management of the Board, in a separate letter dated December 16, 2004.

This report is intended solely for the information and use of the audit committee, management, and Board of Directors, and is not intended to be and should not be used by anyone other than these specified parties.

Roslund, Prestage & Co, PC
Roslund, Prestage & Company, P.C.
Certified Public Accountants

December 16, 2004



MANAGEMENT LETTER

Board of Directors
Manistee-Benzie Community Mental Health Services
Manistee, Michigan

In planning and performing our audit of the financial statements for Manistee-Benzie Community Mental Health Services for the fiscal year ended September 30, 2004, we considered the internal control structure to determine our auditing procedures for the purpose of expressing an opinion on the financial statements and not to provide assurance on the internal control structure.

However, during our audit we became aware of matters that are opportunities for strengthening internal controls and operating efficiency. The memorandum that accompanies this letter summarizes our comments and suggestions regarding those matters.

This letter does not affect our audit report dated December 16, 2004 on the financial statements of Manistee-Benzie Community Mental Health Services.

We will review the status of these comments during our next audit engagement. We have discussed these comments and suggestions with management, and will be pleased to discuss them in further detail at your convenience, to perform any additional study of these matters, or to assist you in implementing the recommendations.

Sincerely,

Roslund, Prestage & Co, PC

Roslund, Prestage & Company, P.C.
Certified Public Accountants

December 16, 2004

STATUS OF PRIOR YEAR RECOMMENDATIONS

During the audit we were pleased to note that all of the recommendations identified in the management letter Manistee-Benzie Community Mental Health Services (the Organization) from the prior year had been reviewed and implemented. We commend you on your efforts to strengthen internal controls and operating efficiencies.

CURRENT YEAR COMMENTS

Perform a Fraud Risk Assessment

In light of the wave of notorious frauds involving large companies in the last few years, such as Enron, WorldCom, and HealthSouth, there may be a misperception that fraud affects only large companies. However, fraud occurs in companies of all sizes, and almost any employee may be capable of perpetrating a fraudulent act given the right set of circumstances. In fact, fraud may be a more significant problem for small companies. In the 2002 survey of its members conducted by the Association of Certified Fraud Examiners (ACFE), the median loss per fraud occurrence reported from businesses with 100 or fewer employees was \$127,500, a proportionately larger loss than the \$97,000 median loss in companies with 10,000 or more employees.

Whereas the highly publicized frauds at large public companies like Enron, WorldCom, and HealthSouth involved fraudulent financial reporting, for small companies, one of the primary fraud risks is the ever-present risk of misappropriation of assets (theft), particularly fraudulent cash disbursements. The opportunity to commit and conceal fraud exists where there are assets susceptible to misappropriation and there are inadequate controls to prevent or detect the fraud. To address this risk, we recommend that the Organization perform a risk assessment to identify, analyze, and manage the risk of asset misappropriation. Risk assessment, including fraud risk assessment, is one element of internal control. Thus, ideally, the Organization's internal control should include performance of this assessment, even though our annual financial statement audit includes consideration of fraud.

Perform a Fraud Risk Assessment (continued)

The fraud risk assessment can be informal and performed by a management-level individual. Ordinarily, the management-level individual would conduct interviews or lead group discussions with personnel who have extensive knowledge of the Organization, its environment, and its processes. The fraud risk assessment process should consider the Organization's vulnerability to misappropriation of assets. When conducting the self-assessment, questions such as the following can be considered:

- Which individuals in the Organization have the opportunity to misappropriate assets? These are individuals who have access to assets susceptible to theft and to records that can be falsified or manipulated to conceal the theft.
- Are there any known pressures that would motivate individuals with the opportunity to misappropriate assets? Pressures may relate to financial stress or dissatisfaction. In assessing whether these pressures may exist, the assessor should consider whether there is any information that indicates potential financial stress or dissatisfaction of individuals with access to assets susceptible to misappropriation.
- What assets of the Organization are susceptible to misappropriation?
- Are there any known internal control weaknesses that would allow misappropriation of assets to occur and remain undetected?
- How could assets be stolen? Assets can be stolen in many ways besides merely removing them from the premises. For example, cash can be stolen by writing checks to fictitious individuals or vendors and cashing them for personal use. Inventory or other assets can be stolen through sales to fictitious customers.
- How could potential misappropriation of assets be concealed? Because many frauds create accounting anomalies, the perpetrator must hide the fraud by running it through the Organization's general ledger as an adjustment to another account. Generally, fraud perpetrators may use general ledger accounts that are not closely monitored.
- What factors might indicate that the Organization has a culture or environment that would enable management or individuals to rationalize committing fraud?

Perform a Fraud Risk Assessment (continued)

Once areas vulnerable to fraud have been identified, a review of the Organization's systems, procedures, and existing controls relating to the identified areas should be conducted. The Organization should consider what additional controls need to be implemented to reduce the risk of fraud. There are two basic types of controls—those that are designed to address specific types of fraud, and those that are more general in nature. General controls that reduce an individual's ability to commit fraud without detection include the following:

- Requiring Periodic Job Rotation and Mandatory Vacations. When an employee stays in the same position for a long period and has few absences, an opportunity exists for that employee to design and commit fraud schemes. Requiring key individuals to rotate jobs periodically or to transfer to different job functions is one way to address this fraud risk. Requiring all individuals to take an annual vacation, during which time others perform their job functions, also makes it more difficult for an employee who is committing fraud to continue concealing the fraud scheme.
- Preparing and Reviewing Monthly Financial Statements in a Timely Fashion. As previously mentioned, many frauds create accounting anomalies. Thus, one way to detect fraud on a timely basis is to review monthly financial statements and investigate unusual variances. If possible, these statements should include budget, prior period, and year-to-date amounts to help identify variances. Performing the review and investigation on a timely basis helps minimize the extent of potential fraud.
- Implementing an Employee Hotline. Tips and complaints from fellow employees or vendors have enabled many companies to discover occurrences of fraud. Anonymous telephone hotlines allow honest employees and vendors who may fear retaliation from fraud perpetrators to report unethical behavior without risking exposure.

Examples of controls to prevent or detect specific types of fraud include the following:

- Independent Checks of work performed. Independent checks test another employee's work, such as by having a second employee re-perform or test an employee's work.
- Separation of Duties. Separation of duties is one of the most effective controls to prevent or detect misappropriations of assets. When possible, incompatible duties should be performed by different employees. For example, the responsibility for authorizing transactions, recording transactions, and maintaining custody of assets should be assigned to different people in the Organization to the extent possible.

Perform a Fraud Risk Assessment (continued)

When assessing the Organization's internal control, the relationship between the nature and extent of fraud controls recommended and the cost of implementing those controls should be considered. For example, instead of trying to prevent fraud, the Organization may choose to use more detective controls to ensure that the fraud is identified and corrected in a timely fashion. Because detective controls are performed after the original transaction occurs, they may be easier to implement and more cost effective.

We would be pleased to provide more information about performing a risk assessment or assist management in performing one.

Perform Surprise Payroll Pay-outs

As a precaution against the use of fictitious employees, we recommend that the finance manager perform periodic surprise pay-outs at various locations of the Organization. This will require the finance manager to distribute pay checks to each employee and to verify identification. If an employee is sick or on vacation during the pay-out, that check should be held for the employee in a safe. When the employee returns, the check should be given by the finance manager to the employee.

Review Payroll Records for Unusual Matters

Performing a careful review of the payroll register (that is, the schedule showing the calculation of gross pay, deductions, and net pay) and payroll check register can highlight several types of payroll fraud. We recommend that an appropriate person independent of the payroll department periodically make such a review, being alert for unusual matters that might suggest fraud, such as the following:

- Duplicate names or addresses.
- Names of former employees.
- Math errors (which may indicate diversion of payroll or payroll taxes).
- Unusual pay rates or numbers of hours worked.
- Factors that may indicate ghost employees.